ILEC commenters go even further and suggest that the Commission adopt a concept of cost based on Fully Distributed Cost ("FDC") methodology for transport and termination. FDC, however, includes not only common costs and overheads, but also embedded costs that are plainly impermissible costs for any calculation of additional costs for reciprocal transport and termination. The plain language of the statute does not permit inclusion of costs that would be incurred regardless of whether a carrier provided the requested transport and termination. Embedded costs, by definition, are already incurred and cannot be treated as "additional costs" of any future transaction.

While ILECs acknowledge, as they must, that bill and keep is an acceptable arrangement, they argue that bill and keep need only be made available if an individual ILEC "voluntarily" waives its rights to payment of additional costs and agrees to the arrangement.[54/] The statute, however, does not require such a "voluntary" waiver.

First, the bill and keep language plainly cannot be intended to apply only to negotiated, voluntary agreements because it is contained in the part of the statute concerning pricing standards to be used in arbitrations, not in the section concerning negotiated agreements.[55/] Second, there was no need for Congress to expressly permit the voluntary use of bill and keep. Given the predominance of bill and keep as an ILEC interconnection arrangement, it is highly unlikely that a State, in its review of a negotiated, voluntary bill

54/ See, e.g., Comments of SBC at 52; Comments of Ameritech at 78-79; Comments of Bell Atlantic at 41; Comments of USTA at 79.

55/ Section 252(a)(1) and (e)(2) govern the submission of voluntary, negotiated agreements to State commissions that are judged under Section 252(e)(2)(A)'s non-discriminatory, public interest standard. In contrast, the Section 252(d)(2) pricing standard that contains bill and keep as an appropriate mechanism is the section that States are required to apply in judging the compliance of an ILEC with Section 251(b)(5) in an arbitration.

and keep agreement, would determine that such an agreement did not satisfy the non-discrimination and public interest tests that States must apply under Section 252(e)(2)(A).

Finally, basic statutory construction principles require that the Commission give effect to each part of the statute. Permitting ILECs to select, on a case-by-case basis, with whom they will voluntarily exchange traffic on a bill and keep basis would not only be blatantly anticompetitive, it also would render the Section 252(d)(2) instruction expressly permitting bill and keep — as an arbitration outcome — meaningless.

The ILEC opposition to bill and keep reflects their deep antipathy towards opening their monopoly markets. While ILECs have uniformly opposed bill and keep in State after State and in the Commission's proceeding to reform LEC-to-CMRS interconnection practices, they have never responded to the compelling argument that bill and keep is a good approximation of what actually would be charged in a competitive free market where the negotiating parties have equal bargaining power.[56/] They have failed to rebut evidence that the incremental cost of reciprocal transport and termination is extremely low, and is most likely offset by the expense of litigating actual costs and the administrative expenses inherent in creating the capability to measure and bill calls. They also have failed to establish that the Commission or the States lack authority to use bill and keep as a rate proxy for reciprocal transport and termination of traffic.

56/ See "Price Structure Issues in Interconnection Fees," by Gerald W. Brock, prepared for Teleport Communications Group, March 30, 1995. (Discussing that bill and keep is used by commercial internet providers and that the "best existing example of interconnection under competitive conditions without regulation is the interconnection of commercial providers of internet services.")

Moreover, ILEC arguments that mandating bill and keep would be an unconstitutional taking are wrong.[57/] Under either of the two standards the courts use to determine whether a taking has occurred, there is no taking in a bill and keep regime.

The first standard is whether there is a physical invasion of private property.[58/] While some LECs suggest that transport and termination is a physical invasion, that is not the case.[59/] Unlike Loretto, for instance, transport and termination does not involve placing the interconnecting carrier's property on ILEC property. It merely involves transmission of information from one network to another.[60/] In addition, even if there were a physical invasion, ILECs would be compensated under a bill and keep regime because they obtain the benefits of being able to terminate calls on the other carrier's network and of being able to receive calls that their customers want.

The other strand of takings jurisprudence — regulatory takings — is equally inapplicable to Cox's bill and keep proposal. A party asserting a regulatory taking bears a heavy burden and must prove that the regulation has a heavy economic impact and interferes with reasonable investment-backed expectations.[61/] For a taking to occur, the economic

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57/ See, e.g., Comments of Bell Atlantic at 40-43; Comments of BellSouth at 71-75; Comments of GTE at 56-59; Comments of USTA at 78-84.

58/ See Loretto v. Teleprompter Manhattan CATV Corp., 458 U.S. 419 (1982); Dolan v. City of Tigard, 114 S.Ct. 2309 (1994).

59/ See Comments of U S West at 29-32.

60/ Thus, the D.C. Circuit's physical collocation decision, which involved a government mandated physical occupation of LEC property, does not apply to bill and keep. Bell Atlantic v. FCC, 24 F.3d 1441 (D.C. Cir. 1994)

61/ Penn Central Transportation Co. v. United States, 438 U.S. 104 (1978) ("Penn Central").

impact of a regulation must be so high as to render the property virtually worthless.[62] The loss of anticipated profits, for instance, is not sufficient to create a regulatory taking.[63] The underlying principle of regulatory takings law is that "[g]iven the propriety of the governmental power to regulate, it cannot be said that the Taking Clause is violated whenever legislation requires one person to use his or her assets for the benefit of another."[64]

Under this standard, Cox's bill and keep proposal does not create a regulatory taking. As Cox previously has demonstrated, the incremental cost of a bill and keep arrangement for transport and termination is extremely low.[65] If the balance of traffic is roughly equal, the benefit to the ILEC of being able to terminate calls on CLEC networks will keep pace with the increased cost, if any, of terminating calls that originate on competing networks. Indeed, as State commissions have found, the imposition of bill and keep will not result in an unconstitutional taking.[66] Equally important, the Cox model provides a specific mechanism

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62/ See Connolly v. PBGC, 475 U.S. 211, 223 (1986) ("Connolly"); Lucas v. South Carolina Coastal Council, 112 S.Ct. 2886, 2893 (1992); see also Penn Central, 438 U.S. at 136.

63/ See Andrus v. Allard, 444 U.S. 51, 66 (1979) ("loss of future profits — unaccompanied by any physical property restriction — provides a slender reed upon which to rest a takings claim")

64/ Connolly, 475 U.S. at 223.

65/ See Dr. Gerald W. Brock — Incremental Cost of Local Usage, March 1995 filed in CC Docket 94-54 on March 21, 1995.

66/ See, e.g., Washington Utilities and Transportation Commission v. U S West Communications, Inc., Fourth Supplemental Order Rejecting Tariff Filings and Ordering Refiling; Granting Complaints, in Part, Docket UT-941464 (released October 31, 1995) at 35 ("Bill and keep is not a system of interconnection 'for free'. Bill and keep is compensatory. There is a reciprocal exchange of traffic in which each company receives something of value.").

for an ILEC or any other carrier with excess inbound traffic to demonstrate and recover its incremental costs of transport and termination, which could be used if, for instance, a carrier is required to expand its capacity to accommodate increasing traffic received from another carrier.

Finally, Pacific Telesis argues that any rate that does not permit recovery of embedded costs is confiscatory.[67/] This claim misstates and misapplies the law of ratemaking. Under those principles, rates are judged against "a zone of reasonableness" which is "bounded at one end by the investor interest against confiscation and at the other by the consumer interest against exorbitant rates" and the constitutionality of authorized rates is based on whether the financial integrity of the company as a whole is threatened.[68/] There never has been a requirement that a particular rate be compensatory, as is evidenced by LEC claims that some of their existing rates are below cost and subsidized by other rates. The ILECs also have provided no evidence that a bill and keep regime for transport and termination, and particularly a regime such as that proposed by Cox that would permit a carrier to demonstrate that it had incurred additional costs, would threaten their financial integrity. They have not even made the case that they will incur *any* additional costs or that they will be unable to recover those costs from other sources. Accordingly, the argument that bill and keep cannot be mandated because it would be confiscatory is flatly contrary to both law and fact.

67/ Comments of Pacific at 66-67.

68/ Washington Gas Light v. Baker, 188 F.2d 11, 15 (D.C. Cir. 1950), cert. denied, 340 U.S. 952 (1951); FPC v. Hope Natural Gas, 320 U.S. 591, 605 (1944). In this inquiry, a court considers the final result of regulation, not the method used to reach that result. Id.

B. TSLRIC and FDC Are Appropriate Boundaries for Prices for Unbundled Elements and Section 251(c) Interconnection. (Notice Section II.B.2.)

As discussed in Cox's comments, TSLRIC and FDC, while violative of the statutory cost standards for reciprocal transport and termination, do satisfy the statutory standard for the States to apply in arbitrations to "bracket" acceptable ILEC pricing of unbundled elements and associated Section 251(c) interconnection. Under Section 252(d)(1), ILECs are entitled to recover their costs, and may also be permitted to recoup a reasonable profit, for unbundled elements. Both TSLRIC and FDC already include profit elements, and thus would guarantee an ILEC a reasonable return on its investment. In addition, TSLRIC and FDC would result in a greater cost recovery to the ILEC than a LRIC cost methodology. Applying a more generous cost standard to the provision of unbundled element services than to transport and termination not only reflects Congressional intent, it also is reasonable because the only benefit the ILEC derives from a carrier purchasing these services is the price paid for the unbundled elements and associated interconnection. This is in contrast to the mutual exchange of benefits received and provided by the reciprocal transport and termination of traffic, where the ILEC receives something of value in exchange for making its network available for transport and termination.

1. Incumbents' Objections to TSLRIC Reflect Inconsistent and Uneconomic LEC Expectations Regarding Recovering the Costs of Their Networks.

Several ILECs object to using TSLRIC-based methodologies for recovering the costs of interconnection and unbundled network elements. These LECs claim that prices set at

TSLRIC would be inconsistent with the 1996 Act[69/] or would disallow recovery of embedded historic costs purportedly necessary for continued LEC operations.[70/] The Commission should reject these arguments because they are inconsistent with the actual requirements of the 1996 Act.

First, TSLRIC is consistent with the 1996 Act. The statute provides little direction on how Section 252(d)(1) "cost" is to be determined except that it directly disavows rate-of-return based rates, *i.e.*, the regulatory regime which allowed automatic recovery of historic costs.[71/] Thus, there is nothing in Section 252(d)(1) that precludes the use of TSLRIC or requires that any historic costs be recognized.[72/]

Although some LECs claim that TSLRIC is constitutionally infirm, there is no constitutional entitlement for a regulated entity to recover historic costs.[73/] In particular, the Supreme Court has held that the due process clause "has not and cannot be applied to insure values . . . that have been lost by the operation of economic forces."[74/] Indeed, no LEC points to any case that requires recovery of embedded costs.

69/ See Comments of GTE at 76; Comments of USTA at 43-50.

70/ See Comments of Cincinnati Bell at 30-31; Comments of BellSouth at 57.

71/ 47 U.S.C. § 252(d)(1)(A).

72/ Indeed, TSLRIC is consistent with the Commission's own goal of pricing that "replicates market-based incentives and prices." See, e.g., Notice of Proposed Rulemaking, Interconnection Between Local Exchange Carriers and Commercial Mobile Radio Service Providers, Dkt. No. 98-185, FCC 95-505 at ¶ 4.

73/ Comments of PacTel at 69-70; Comments of USTA at 47.

74/ Market St. Ry. Co. v. Railroad Comm. of California, 324 U.S. 548, 567 (1945)("Market St. Ry.").

Furthermore, the LECs are in no position to claim that they have any expectation of recovering their historic costs. Over the last several years many LECs have written down their telephone assets. These write-downs occurred because the LECs claimed that they did not expect to recover the full costs of deploying their networks in anticipation of competitive networks.[75/] They cannot now claim to have an expectation that historic costs will be recovered, especially because investor expectations — the only expectations that matter — should have been adjusted in light of the write-downs.

Moreover, ILECs already have recovered a substantial portion (if not all) of their embedded costs. Even accepting the USTA claim that the adoption of TSLRIC would result in under-recovery of between $13 and $17 billion in embedded costs (an amount that is less than the anticipatory writedowns ILECs already have taken), these figures would constitute only a small fraction of the profits that LECs have earned. Over the past ten years, for example, the profits of the BOCs and GTE have exceeded $70 billion.[76/] In light of these substantial and recurring returns, the LECs have no entitlement to additional returns on embedded costs in the future

In addition, despite the incumbents' criticism of TSLRIC, there is no guarantee that TSLRIC in any particular case will yield a result less than FDC. The relative level of TSLRIC and FDC will depend on many factors, such as the relative costs of inputs.[77/]

75/ Based on the SEC filings of the RBOCs and GTE, these writedowns exceed a total of [$23] billion.

76/ This figure is based on review of the SEC filings of the RBOCs and GTE. Absent the writedowns noted above, total profits would have exceeded $93 billion.

77/ For instance, services that an incumbent provides that depend upon highly-depreciated assets may have relatively low fully distributed costs. In addition, some inputs used to provide a service, such as labor, are more expensive today than they would have

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Finally, the Cox model, which uses TSLRIC only as a boundary, does not inflexibly constrain LECs from making a case that they should recover amounts over and above TSLRIC. Where an incumbent can show that TSLRIC would not be sufficient, it will have the opportunity to persuade a State commission that prices for unbundled elements should be calculated using FDC.[78/] This will permit each State to make its own determination as to the appropriate level of incumbent cost recovery for unbundled elements.

2. There Is No Reason to Permit LECs to Recover More than the Fully Distributed Cost of Unbundled Elements.

Some ILECs suggest that the Commission should adopt a standard for pricing unbundled elements that permits them to recover their embedded costs plus some additional amount, either as "profit" under Section 252(d)(1) or on the basis of foregone monopoly revenues in the future.[79/] There is no rationale to permit such an approach.

First, it is important to recognize that, as an absolute cost ceiling, FDC more than compensates a LEC for any cost it reasonably could expect to recover. FDC is based on embedded costs, *i.e.*, the costs the LEC has incurred, and includes profits calculated using embedded costs. Incumbent LECs have no legal entitlement to more than that.[80/] Moreover,

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77/ (...continued)
been in the past. For services dependent upon these more expensive inputs, TSLRIC may lead to costs that are higher than FDC.

78/ While States should have the latitude to determine that some or all costs for unbundled elements should be based on recovery of embedded costs, Cox envisions that FDC would be the exception, rather than the generally applied standard.

79/ See, e.g., Comments of BellSouth at 56-57; Comments of Cincinnati Bell at 30-31; Comments of USTA at 47.

80/ Indeed, any price that exceeds fully distributed cost is likely to be too high and, consequently, legally impermissible because it exceeds the bounds of the zone of

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as shown above, many incumbent LECs already have informed shareholders that they do not expect to recover all of their embedded costs by writing down the financial book value of their telephony assets.[81] Consequently, FDC is the absolute ceiling of what a LEC could reasonably expect to recover for unbundled elements or for Section 251(c) interconnection; any greater cost recovery would constitute an unjustified windfall.

The incumbent LECs' claim to arbitrated prices for unbundled elements that exceed FDC apparently is based on the presumption that incumbents must be made whole by their competitors for the impact of competition. As a legal matter, this is simply untrue — previous regulation is never a guarantee of future profits and the law does not protect a competitor from the effects of lawful competition.[82]

The idea that incumbents should be entitled to recover the monopoly profits they will lose as a result of competition is derived from the discredited efficient component pricing rule (the "ECPR").[83] Despite the Commission's tentative rejection of ECPR as a credible pricing method, several incumbents spend considerable effort in an attempt to rehabilitate

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80/ (...continued)
reasonableness. See Washington Gas Light v. Baker, 188 F.2d 11, 15.

81/ See supra page 25. In addition, BellSouth suggests that embedded cost and book cost are, in fact, the same. Comments of BellSouth at 56. To the extent that this is true, the written-down values of telephony assets on the companys' financial books would be the correct ones to use to determine embedded cost, not the values on LECs' regulatory books.

82/ See Market St. Ry., 324 U.S. at 566.

83/ The ECPR holds that a monopolist should be able to recover all of its expected monopoly profits from its competitors if those competitors must obtain some elements of their service from the monopolist. The Notice correctly rejects the ECPR as an unreasonable pricing theory. Notice at ¶ 148.

it.[84/] Cox concurs with the comments filed by Professor Nicholas Economides, that demonstrate that ECPR effectively prohibits competition by making the bottleneck market a legal monopoly, whether or not it is a natural monopoly.[85/]

Finally, certain LECs suggest that the 1996 Act requires an explicit add-on profit element *above* FDC because Section 252(d)(1) mentions "profit" separately from "cost." The statute does not support this claim. First, "cost," as States and the Commission have applied the economic theory of TSLRIC and FDC, includes a return on capital. Clearly a return on invested capital is profit. Second, the statute does not require the inclusion of any profit at all — let alone the recovery of profit — in addition to the profits already reflected in either an FDC or TSLRIC methodology.[86/] It is ludicrous to suggest that Congress intended to entitle incumbent LECs to receive monopoly profits above and beyond the return on legacy investment. The goal of the 1996 Act was to benefit consumers by encouraging the development of competition in the local telephone market.[87/]

84/ GTE even attaches a "redacted" report rearguing the virtues of ECPR. See "An Empirical Analysis of Pricing Under Sections 251 and 252 of the Telecommunications Act of 1996," by Michael Doane, J Gregory Sidak and Daniel Spulber.

85/ See Comments of Professor Economides at 6.

86/ See 47 U.S.C. § 252(d)(1)(B) (prices "may include a *reasonable* profit") (emphasis added).

87/ See S. Conf. Rep. No. 104-230, 104th Cong., 2d Sess. 1 (1996) at 1. (1996 Act is intended "to provide for a pro-competitive, de-regulatory national policy framework" that brings improved services "to all Americans by opening all telecommunications markets to competition").

C. The Commission Should Adopt Proxies as Defaults for Arbitrations. (Notice Section III.A.)

In addition to adopting boundaries for cost determinations under Section 252(d)(1) and Section 252(d)(2), the Commission also should adopt specific proxies that the States can use as defaults in arbitrations. As the 1996 Act suggests, proxies should not be derived from current ILEC rates, but instead should be based on reasonable approximations of their costs. Bill and keep is an appropriate proxy for the additional cost reciprocal transport and termination, while some form of the costing models mentioned in the Notice and by the Department of Justice could be adopted as a proxy for unbundled elements and associated Section 251(c) interconnection.

Proxies are appropriate for several reasons. First, they implement Congressional intent to base compensation on costs without resorting to traditional rate of return or intensive cost studies that depend upon easily manipulated LEC cost data.[88/] Second, they will reduce the burdens of arbitrations on the States. Reducing implementation burdens may be very important to States which have limited resources or which face numerous arbitrations.[89/]

Third, proxies will help to encourage good faith negotiations. In essence, proxies define "preferred outcomes" for negotiations, a technique that has been found useful by some States.[90/] Finally, proxies also give the parties something to bargain away from if they so

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88/ See 47 U.S.C. § 252(d)(1)(A)(i), (2)(B)(ii).

89/ Indeed, some states are expressing concern about their ability to implement the 1996 Act. See Comments of North Dakota at 1; see also Implementation of the Telecommunications Act of 1996, Tentative Decision, Pa. Pub. Util. Comm., Docket No. M-009 (Mar. 14, 1996), at 5-8.

90/ Comments of PacTel at 94.

desire. For instance, a new entrant might agree to transport and termination compensation that exceeds the proxy in return for favorable rates for collocation or unbundled loops. Giving both parties additional "bargaining chips" through the adoption of proxies will greatly enhance the ability of the parties to reach an agreement.

The Commission can achieve these benefits, however, only by defining specific proxies. The proxies should be based on approximate, forward looking costs, and should not be based on current prices for access or other LEC services.[91/] Using approximate forward looking costs is consistent with the requirements of the 1996 Act and also prevents incumbents from obtaining bargaining leverage from insisting on proxies that are set too high.[92/]

This approach makes bill and keep the ideal proxy for reciprocal transport and termination because it is a good approximation of actual costs. As Cox and others have established, the actual costs of transport and termination are quite low.[93/] At the same time, if traffic is in balance (or close to balance) the net cost of obtaining transport and termination

91/ Access rates are a particularly poor proxy because, as even incumbent LECs concede, they far exceed cost. Any effort to remove the non-cost elements from an access-based proxy is far less likely to yield an appropriate rate than will a forward looking cost method. Comments of Cox, Exhibit 3, Brock Statement at 6. Moreover, existing access rates were determined using rate of return methodologies, which is inconsistent with the 1996 Act's cost standards. 47 U.S.C. § 252(d)(1)(A)(i), (2)(B)(ii).

92/ 47 U.S.C. § 252(d). If proxies are too high, incumbent LECs will gain additional bargaining leverage. The risks of setting a proxy too low, on the other hand, are small. Not only do new entrants have very little bargaining leverage to begin with, but a proxy that is too low will create an incentive for the incumbent LEC to produce the information necessary to support a more accurate cost determination. If the proxy is too high, it is unlikely that the incumbent would ever produce contrary information.

93/ See "Incremental Cost of Local Usage" by Dr. Gerald W. Brock, filed in Dkt. No. 94-54 on Mar. 21, 1995; Comments of NCTA at 55; Comments of TCI at 35-38.

is zero (or minuscule), regardless of the actual cost for each unit of capacity.[94] Thus, bill and keep is likely to approximate the results of any objective determination of the costs of transport and termination.

The Commission also should adopt a cost-based proxy for the costs of unbundled elements and Section 251(c) interconnection. A TSLRIC based cost model, such as BCM or the Hatfield model, would be ideal. Most important, models allow for variation from carrier to carrier and geographic area to geographic area because the inputs can be varied. This avoids the problem of "one-size-fits-all" pricing that concerns some commenters.[95] At the same time, use of a model such as the Hatfield model that is largely or entirely based on publicly-available inputs (such as ARMIS data) will permit any interested party to evaluate relevant incumbent costs, which will aid them in negotiations.

III. THE COMMISSION MUST DEFINE BASIC TERMS AND CONDITIONS FOR NEGOTIATIONS UNDER SECTIONS 251 AND 252. (Notice Section II.B.2, Section II.C.5, Section II.C.2.e.2, Section II.B.1, Section II.C and Section III)

A. The Commission Should Not Permit the Imposition of Separate Interconnection Charges on Carriers Reciprocally Exchanging Traffic for Transport and Termination. (Notice Section II.B.2 and and Section II.C.5

The Commission must straightforwardly establish that reciprocal compensation for the exchange of traffic between a facilities-based competitor and an ILEC is not conditioned on any separate Section 251(c) interconnection charge. Contrary to the assertions of some ILECs, transport and termination for the mutual exchange of traffic is a self-contained

94/ Comments of MCI at 51-53.

95/ See, e.g., Comments of PacTel at 26.

transaction that is governed exclusively by Sections 251(b)(5) and 252(d)(2).[96/] There is no hint of a separate or conditional add-on interconnection charge in these provisions. If Congress had intended for carriers to include a separate, cost-plus interconnection charge in the transport and termination of traffic, it would have incorporated such a provision into the terms of the statute.[97/]

In reality, moreover, most ILECs do not include a separate interconnection charge in providing transport and termination for the mutual exchange of traffic with neighboring LECs.[98/] It would be unreasonably discriminatory for incumbent LECs to assess a separate interconnection charge against competing LECs for transport and termination of traffic when no similar charge is required in the neighboring LEC-to-LEC context.

There is also no practical basis for assessing a separate "interconnection" charge. In practice, many reciprocal compensation arrangements will employ meet point technologies that, of necessity, will be the same for both parties. The MCI-BellSouth interconnection agreement, for example, has no separate interconnection charge for its transport and termination arrangements.[99/]

Finally, the ILECs cannot insist on collecting any separate interconnection charge that is based on any costs they identify as "residual" or "legacy" costs. Recovery of revenue

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96/ See 47 U.S.C. §§ 251(b)(5), 252(d)(2).

97/ It is well-settled that, when "the statute speaks with crystalline clarity . . . .[,] it is not necessary to look beyond the words of the statute." See American Civil Liberties Union v. FCC, 823 F.2d 1554, 1568 (D.C. Cir. 1987) (quoting TVA v. Hill, 437 U.S. 153, 184 n.29, 98 S.Ct. 2279, 2296 n.29 (1978) (emphasis in the original)).

98/ See Michigan Exchange Carriers Association at 19; Comments of Ameritech at 96.

99/ See BellSouth and MCI Sign Key Interconnection Pact Running 2 Years, COMM. DAILY, May 17, 1996, at 3.

shortfalls that occur as a result of competition plainly are anticompetitive and do not comport with the incremental cost-based pricing parameters set forth in Section 252(b)(2) for transport and termination of traffic.[100/]

B. The Commission Should Adopt Specific Minimum Technical Standards. (Notice Section II.B.2 and Section II.C.5)

The comments demonstrate there is a real need for minimum standards for the technical terms of interconnection. ILECs urge the Commission either to avoid standards or to adopt rules that let incumbents decide what types of interconnection they wish to provide. These proposals are contrary to the statute and would impede the development of facilities-based competition.

ILECs support approaches that would greatly limit the ability of new entrants to obtain technically feasible interconnection. For instance, USTA and several ILECs advocate a so-called "*bona fide* request" process that would give them the freedom unilaterally to determine what is "technically feasible" and to engage in anticompetitive delay tactics.[101/] Some LECs also suggest that each interconnection request should trigger a new inquiry into whether the specific points of interconnection are technically feasible.[102/] Either of these approaches would unnecessarily complicate the interconnection process and would permit

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100/ Expanded Interconnection with Local Telephone Company Facilities, 9 FCC Rcd. 5154, 5158 (1994). This approach does not preclude interconnection charges when a connecting carrier purchases unbundled elements, or charges for collocation, which would be handled under Sections 251(c) and 252(d)(1).

101/ The USTA proposal would also short-circuit a requesting telecommunications carrier's right to due process in filing a State arbitration petition by requiring that "the *bona fide* request process [itself] . . . provide a basis for reasoned judgment should either party elect arbitration." Comments of USTA at 13 - 15.

102/ See, e.g., Comments of BellSouth at 15; Comments of NYNEX at 64.

ILECs to decide when and where they would interconnect, despite the statutory requirement for interconnection wherever technically feasible. All of these proposals are consistent with the Notice's observation that LECs may "already have employed certain tactics that the Commission should determine violate the duty to negotiate in good faith."[103/]

To prevent ILEC intransigence regarding technical terms of interconnection from sabotaging the negotiation and arbitration process, any existing arrangements used by the incumbent LEC (including meet points) should be deemed technically feasible absent clear and convincing evidence to the contrary.[104/] This minimum standard for technical feasibility must apply in determining points of interconnection for purposes of both Section 251(c)(2) and Section 251(b)(5).[105/] The Commission also should adopt minimum quality standards, such as those proposed by Teleport Communications Group, including standards for mid-span meet points and two-way trunking.[106/] Adopting specific standards will speed the resolution of negotiations and prevent incumbent LECs from exploiting market power to undermine negotiation and performance of agreements.[107/]

Finally, minimum standards will not prevent parties from reaching other arrangements if they so desire. Parties are free, pursuant to Section 252(a)(1), to negotiate arrangements that fail to meet or that exceed the minimum standards. As Cox proposed in its comments

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103/ See Notice at ¶ 47.

104/ As the Notice correctly concludes, "a particular point will be considered technically feasible . . . if an incumbent LEC currently provides, or has provided in the past, interconnection to any other carrier at that point . . . ." Notice at ¶ 57.

105/ Of course, parties will remain free, pursuant to Section 252(a)(1), to negotiate arrangements that fail to meet or to exceed the minimum standards.

106/ See Comments of Teleport Communications Group at Appendix A.

107/ See id.

in this proceeding, moreover, adopting minimum technical standards avoids the problem of adopting a generic standard that may not be appropriate for all LECs.[108]

C. Sections 251 and 252 Do Not Cover All Aspects of LEC-to-CMRS Interconnection. (Notice Section II.C.2.e.2)

Section 332(c) of the Act is the lodestone for a CMRS provider's right to interconnection and reciprocal compensation to LEC networks on just, reasonable and nondiscriminatory rates, terms and conditions. Nothing in the 1996 Act deprives CMRS providers of these rights and Section 251 is insufficient on its own to assure that CMRS providers will obtain reasonable and timely interconnection. For example, applying the exemption from interconnection obligations in Section 251(f) for rural and small telephone companies in the LEC-to-CMRS interconnection context would prevent a CMRS provider from obtaining interconnection to which it is otherwise entitled under Section 332(c). For this and the reasons Cox has previously provided, the Commission should determine that Section 332(c) is an independent basis for Commission action on LEC-to-CMRS interconnection.

D. The Commission Must Adopt Rules that Prevent "Pattern Bargaining" by Incumbent LECs. (Notice Section II.B.1)

The 1996 Act contemplates individual negotiations between incumbents and new entrants over the terms of interconnection and unbundling. The 1996 Act did not envision one interconnection contract negotiated between an incumbent LEC and a new entrant that precluded variations by other entrants. In order to further the good faith negotiation process,

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108/ See Comments of Cox at 42-43.

the Commission should expressly recognize that such "pattern bargaining" is evidence of bad faith negotiations under Section 251 and 252.[109]

There will be differences among the entities that seek to negotiate agreements under Section 251 and 252. Cox's needs may be very different from those of AT&T or MFS. Each carrier's needs will depend upon its business plans, the technologies used to interconnect or collocate facilities and its costs of providing transport and termination to the ILEC. Even the ILECs recognize that there will be differences among interconnectors.[110] Nevertheless, there already is evidence that some LECs intend to engage in pattern bargaining, ranging from U S West's "model" interconnection agreement to the highly detailed "*bona fide* request" process proposed by USTA.

Congress already has addressed this concern. Just as the Section 252(i) non-discrimination provision protects a new entrant's ability to take a previously negotiated agreement, Section 252(a) protects an entity's right to forge its own agreement.[111] Consequently, the Commission should make clear that a party who does not wish to agree to specific terms of an existing agreement should be free to negotiate individualized terms for

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109/ Under the pattern bargaining format long used by BOCs affiliates, the BOCs would select two unions with early contract expiration dates and would attempt to reach a settlement with both, which would then be used model contract for other units around the country. See New York Telephone Co. v. New York State Department of Labor, 440 U.S. 519, 522 (1979) (describing pattern bargaining practices of pre-divestiture Bells).

110/ See Comments of BellSouth at 79-82; Comments of GTE at 83; Comments of NYNEX at 90-98; Comments of Pacific Telesis at 100-101.

111/ In this connection, it should be noted that while it may be reasonable for an ILEC to require an entity to take an existing agreement as a whole, the Commission should not permit LECs to require an exact correspondence between two agreements, especially on minor terms such as the exact locations of points of interconnection. See AT&T Revision to Tariff FCC No. 12, 4 FCC Rcd. 4932, 4934, recon. denied, 4 FCC Rcd. 7928 (1989), rev'd. and remanded, MCI v. FCC, 917 F.2d 30, 37 (D.C. Cir. 1990).

interconnection.[112/] The failure of a new entrant to agree to terms already agreed-to by other entities should not be considered evidence of the CLEC's failure to bargain in good faith. Conversely, incumbent LEC insistence on the terms of an existing negotiated agreement should be treated as evidence of failure to bargain in good faith, especially if the incumbent refuses to alter any material terms of the existing agreement.

E. Agreements Between Adjacent LECs Are Within the Scope of the 1996 Act. (Notice Section II.C and Section III)

Several ILECs argue that existing interconnection agreements between adjacent LECs are not covered by the 1996 Act.[113/] This argument is based on a misunderstanding of the new law. Neither Section 251(b)(5) nor Section 252(a) makes any distinction between adjacent carriers and overlapping carriers; indeed, both sections refer only to local exchange carriers and telecommunications carriers.[114/] This equal treatment of adjacent and overlapping carriers is perfectly reasonable because there is no reason to believe that adjacent carriers will treat new entrants any better than overlapping carriers in the interconnection negotiation process. Adjacent carriers have no incentive to encourage new entrants that might someday expand their service areas and, unlike new entrants, they have existing relationships with other incumbents they may wish to preserve.

112/ To this end, State commissions should not be permitted to accept agreements negotiated after the enactment of the 1996 Act as evidence of terms that comply with the relevant statutory and regulatory requirements. The statute specifically permits agreements that do not comply with Section 251 to be effective and State commissions may invalidate these privately negotiated agreements only if they violate Section 252's anti-discrimination requirement.

113/ See, e.g., Comments of SBC Communications at 53; Comments of NYNEX at 9-14.

114/ 47 U.S.C. §§ 251(b)(5), 252(a).

The Commission also should recognize that adjacent carrier agreements are almost as important to new entrants as agreements with overlapping carriers. After all, new entrants' customers will expect to be able to reach the adjacent LECs' customers just as they would if they were customers of the overlapping LEC. At the same time, distinctions between overlapping and adjacent carriers may not be meaningful in the long term. Not only will new entrants' service areas differ from those of incumbents, but it is likely that service areas of both new entrants and incumbents will expand to overlap carriers that previously were only adjacent.[115]

In addition, adjacent carrier agreements are important to new entrants because those agreements provide important information about how incumbent carriers compensate each other for transport and termination of traffic. Adjacent carrier agreements, which were negotiated by parties with relatively equal bargaining power, should provide significant evidence of how freely-negotiated interconnection agreements would be structured.[116] Consequently, not only should these agreements be deemed to provide evidence of reasonable compensation for transport and termination, but new entrants should be permitted to adopt

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115/ For instance, both Pacific Bell and GTE have sought authority to serve each others' service areas in California. See Calif. PUC Kicks Off Local Competition in $7 Billion Market; STATE TEL. REG. REP., January 11, 1996 at 1.

116/ While existing adjacent carrier agreements, which were negotiated before the 1996 Act, are useful evidence of appropriate costs recovery for incumbent LECs, that does not mean that agreements negotiated under the 1996 Act should be given any weight in arbitration. Post-1996 Act agreements between incumbents and new entrants continue to suffer from the infirmities that result from unequal bargaining power, a concern that does not affect existing adjacent carrier agreements.

the terms of any adjacent carrier agreement now in effect or in place in at least the last 24 months preceding the adoption of the 1996 Act, under the provisions of Section 252(i).[117/]

IV. THE COMMISSION SHOULD CONFORM TO CONGRESSIONAL INTENT BY MAINTAINING THE DISTINCTIONS BETWEEN TYPES OF CARRIERS CONTAINED IN THE 1996 ACT. (Notice Section Section II.B)

The 1996 Act imposes varying regulatory obligations on three different types of entities: telecommunications carriers, local exchange carriers and incumbent local exchange carriers. The obligations imposed on the different types of companies are designed to promote Congress' vision of a network of networks that gives consumers a choice of service providers, consistent with its goal of deregulating whenever possible.[118/] Congress recognized that it should impose varying obligations because some companies, in particular incumbent LECs, could not be expected to willingly take the actions necessary to promote competition.

Some States argue and some ILECs agree that they should have the authority to impose on new entrants the requirements that the 1996 Act places only on incumbent LECs.[119/] This position must be rejected as inconsistent with the plain requirements of the 1996 Act and ill-advised from a public policy perspective. No commenter suggests that there is any public benefit from requiring new entrants to comply with the same requirements applicable to incumbents and the incumbents count upon the Commission forgetting its past

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117/ See Comments of Cox at 46.

118/ See Conference Report at 1 (1996 Act is intended "to provide for a pro-competitive, de-regulatory national policy framework" that brings improved services "to all Americans by opening all telecommunications markets to competition").

119/ See, e.g., Comments of Ohio at 6-8; Comments of Louisiana at 2. See also Comments of USTA at 7-8.

rejection of this gambit in the long distance market. Indeed, competition and the public interest are likely to be harmed, since these requirements will raise the costs to potential competitors seeking to enter the local exchange market, and could discourage some entities from entering at all. It is for these reasons that Congress explicitly rejected the notion that there should be complete regulatory parity between incumbents and new entrants. States accordingly should be prohibited from imposing any requirement that violates the distinctions established by Congress.

V. CONCLUSION

For the foregoing reasons, Cox urges the Commission to adopt flexible national standards for local competition that reflect Cox's pro-competitive model.

Respectfully submitted,

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EXHIBIT 1

Glossary of Economic Terms

GLOSSARY OF ECONOMIC TERMS

Long run — A period of time of sufficient length that all inputs can be varied and none is fixed.

Incremental cost — The cost ascribable to any specified change in volume of output or service. Incremental cost is affected by the baseline mix of services; the definition of the increment; and the time frame examined.

Forward-looking costs — Costs based on the options available to the firm at the time they are incurred and which do not account for sunk expenditures.

Embedded costs — Costs that take into account expenditures made in the past.

Long run incremental cost ("LRIC") — The forward-looking cost of any specified change in volume of output or service in the long run. This term should be used in the context of a specific existing output or service. LRIC does not include any overheads. For instance, the cost of adding additional capacity for transport and termination to a carrier's existing capacity for that functionality can be calculated on a LRIC basis. Use of LRIC as a costing standard is appropriate when a firm must recover the additional costs associated with providing specific capacity.

Total service long run incremental cost ("TSLRIC") — The forward-looking cost of adding an entire service to the services offered by a firm in the long run. TSLRIC includes overheads or common costs associated with the service, but does not include general overheads of the firm. For instance, the cost of providing local telephone service can be calculated on a TSLRIC basis. TSLRIC would be an appropriate costing standard when a firm is permitted to recover its reasonable forward-looking costs of providing a product or service.

Fully distributed costs ("FDC") — Costs calculated using a system of cost assignment in which all costs recorded in the books of account, including sunk investment and general overheads, are allocated among products and services, or combinations of categories of products and services. FDC is an embedded cost methodology. Use of FDC as a costing standard is appropriate when a firm is permitted to recover all of the costs it has incurred to provide a product or service.